

11 Am. Jur. 2d Bills and Notes X A Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

A. In General

[Topic Summary](#) | [Correlation Table](#)

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes  425, 426

A.L.R. Library

A.L.R. Index, Bills and Notes

A.L.R. Index, Checks and Drafts

A.L.R. Index, Holder in Due Course

A.L.R. Index, Release or Discharge

A.L.R. Index, Uniform Commercial Code

West's A.L.R. Digest, Bills and Notes  425, 426

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 343

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

A. In General

§ 343. Discharge of obligation on negotiable instrument, generally

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  425

Treatises and Practice Aids

As to discharge availability, effect, and simple contract discharge, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to discharge by agreement, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\): Search Query](#)]

The Uniform Commercial Code is the exclusive means by which obligations under negotiable instruments may be discharged.¹

The obligation of a party to pay an instrument is discharged as stated in the Negotiable Instruments Article² or by an act or agreement with the party which would discharge an obligation to pay money under a simple contract.³

¹ Cumberland Bank v. G & S Implement Co., Inc., 211 S.W.3d 223, 60 U.C.C. Rep. Serv. 2d 736 (Tenn. Ct. App. 2006).

Discharge of a negotiable instrument such as a promissory note is governed by the Uniform Commercial Code. *Haynes v. Dover*, 17 Neb. App. 640, 768 N.W.2d 140 (2009).

² U.C.C. §§ 3-101 to 3-605.

³ U.C.C. § 3-601(a) (2002 Rev).

As to discharge where an instrument is taken for an underlying obligation, see § 117.

As to acts which discharge a simple contract for the payment of money, see § 349.

As to discharge by payment of an instrument, see §§ 351 to 365.

As to discharge by impairment of recourse or collateral, see §§ 369 to 383.

11 Am. Jur. 2d Bills and Notes § 344

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

A. In General

§ 344. Who may discharge obligation on negotiable instrument

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  426

An instrument payable to two or more persons in the alternative is payable to any one of them and may be negotiated, discharged, or enforced by any or all of them in possession of the instrument.¹ The possession required for an alternative payee to discharge an instrument is not limited to physical possession, but extends to items under the payee's dominion and control.²

If an instrument is payable to two or more persons not alternatively, it may be discharged only by all of them.³

Because payment to one nonalternative copayee without the endorsement of the other is not payment to a holder, it does not discharge drawer of either liability on the instrument or underlying obligation.⁴

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-110\(d\)](#) (2002 Rev).

² [Matter of Estate of Walker](#), 473 N.W.2d 45, 15 U.C.C. Rep. Serv. 2d 512 (Iowa 1991).

³ [U.C.C. § 3-110\(d\)](#) (2002 Rev).
As to negotiation of an instrument by multiple payees, see [§ 176](#).

⁴ [McAllen Hospitals, L.P. v. State Farm County Mut. Ins. Co. of Texas](#), 433 S.W.3d 535, 83 U.C.C. Rep. Serv. 2d 683 (Tex. 2014); [ViewPoint Bank v. Allied Property and Cas. Ins. Co.](#), 439 S.W.3d 626, 84 U.C.C. Rep. Serv. 2d 295 (Tex. App. Dallas 2014).

§ 344. Who may discharge obligation on negotiable instrument, 11 Am. Jur. 2d Bills...

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 345

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

A. In General

§ 345. Effect of discharge of obligation on subsequent holder in due course

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  426

Treatises and Practice Aids

As to effect of notice of discharge on holder in due course, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\) Search Query](#)]

Forms

Forms relating to discharge and holder in due course, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\) Search Query](#)]

The discharge of the obligation of a party is not effective against a person acquiring rights of a holder in due course of the instrument without notice of the discharge.¹

Observation:

Implicit in the foregoing provision is the fact that a person who is merely a transferee of the instrument, or a person who is a holder but who does not have the rights of a holder in due course, is subject to the defense that the obligor in question has been

discharged from liability on the instrument.²

Comment:

Discharge is effective against a holder in due course only if the holder had notice of the discharge when holder in due course status was acquired, as where an instrument bearing a cancelled indorsement is taken by a holder.³

The fact that a person taking an instrument has notice of the discharge of an obligor on the instrument does not bar such a taker from being a holder in due course, but only subjects the holder to the defense of that discharge.⁴ Thus, while a person may take an instrument on which one or more signatures have been cancelled and still be a holder in due course, such a holder is barred from enforcing the instrument against any party whose signature was cancelled.⁵

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-601\(b\)](#) (2002 Rev.).

² [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-601:5 \[Rev.\]](#) (3d ed.). As to discharge as a defense, see §§ [553](#), [554](#).

³ [U.C.C. § 3-601](#) (2002 Rev), Official Comment.

⁴ [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-601:6 \[Rev.\]](#) (3d ed.).

⁵ [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-601:6 \[Rev.\]](#) (3d ed.).

11 Am. Jur. 2d Bills and Notes X B Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

[X. Discharge of Obligation](#)

[B. Discharge of Obligation to Pay](#)

[Topic Summary](#) | [Correlation Table](#)

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes  427(.5) to 432, 434, 435, 437, 438

A.L.R. Library

A.L.R. Index, Bills and Notes

A.L.R. Index, Checks and Drafts

A.L.R. Index, Holder in Due Course

A.L.R. Index, Release or Discharge

A.L.R. Index, Uniform Commercial Code

West's A.L.R. Digest, Bills and Notes  427(.5) to 432, 434, 435, 437, 438

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 346

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

1. Discharge Other Than by Payment

§ 346. Discharge of obligation to pay on negotiable instrument by cancellation or renunciation

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435, 437

A.L.R. Library

[What constitutes renunciation by surrender of negotiable instrument under U.C.C. sec. 3-605, 96 A.L.R.3d 1144](#)

Treatises and Practice Aids

As to discharge by cancellation or renunciation, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [\[Westlaw®\(r\): Search Query\]](#)

Forms

Forms relating to renunciation or discharge of maker, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [\[Westlaw®\(r\) Search Query\]](#)

A person entitled to enforce an instrument may discharge the obligation of a party to pay the instrument, with or without consideration, by any intentional voluntary act, such as:¹

- surrender of the instrument to the party
- destruction, mutilation, or cancellation of the instrument
- cancellation or striking out of the party's signature
- addition of words to the instrument indicating discharge
- agreeing not to sue or otherwise renouncing rights against the party by a signed record²

Definition:

"Signed," with respect to a record that is not a writing, includes the attachment to or logical association with the record of an electronic symbol, sound, or process with the present intent to adopt or accept the record.³

Caution:

A discharge of the obligation of a party to pay an instrument under the foregoing provisions does not necessarily discharge the obligation of a secondary obligor having a right of recourse against the discharged party.⁴

Cancellation or striking out of an indorsement does not affect the status and rights of a party derived from the indorsement.⁵ Thus, while the cancellation of an indorsement will renounce all rights against the indorser, it does not break the chain of title through which the person entitled to enforce the instrument owns or holds it.⁶ Furthermore, if the person whose indorsement is cancelled or a prior holder was a holder in due course, the person entitled to enforce the instrument is a holder through a holder in due course, despite the cancellation.⁷

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-604(a) (2002 Rev).

As to discharge of an obligation by payment, see §§ 351 to 365.

As to discharge of an obligation due to a fraudulently made alteration, see §§ 535 to 539.

² *First Commerce Bank v. Dockery*, 171 N.C. App. 297, 615 S.E.2d 314, 59 U.C.C. Rep. Serv. 2d 18 (2005) (a borrower was liable for the debt obligation on a promissory note, despite a coborrower's contention that the lender agreed to release the borrower when the coborrower reaffirmed the debt following bankruptcy, as the alleged release was not in a signed writing).

³ U.C.C. § 3-604(c) (2002 Rev).

⁴ As to the discharge of secondary obligors, see §§ 366 to 385.

⁵ U.C.C. § 3-604(b) (2002 Rev).

⁶ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-604:12 [Rev.] (3d ed.).

⁷ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-604:12 [Rev.] (3d ed.).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 347

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

1. Discharge Other Than by Payment

§ 347. Discharge of obligation to pay on negotiable instrument by cancellation or renunciation—Of claim or right after breach

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435, 437

Treatises and Practice Aids

As to waiver or renunciation of claim or right after breach, see Lawrence's Anderson on the Uniform Commercial Code, Article 1 [Rev] General Provisions [[Westlaw®\(r\): Search Query](#)]

A claim or right arising out of an alleged breach may be discharged in whole or in part without consideration by agreement of the aggrieved party in an authenticated record.¹ A party may authenticate a record by (i) signing a record that is a writing, or (ii) attaching to or logically associating with a record that is not a writing an electronic sound, symbol, or process with the present intent to adopt or accept the record.²

Comment:

This section makes consideration unnecessary to the effective renunciation or waiver of rights or claims arising out of an alleged breach of a commercial contract where the agreement effecting such renunciation is memorialized in a record authenticated by the aggrieved party. These provisions, however, must be read in conjunction with the code provision which imposes an obligation of good faith.³

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 1-306](#).

² [U.C.C. § 1-306](#), Official Comment.

³ [U.C.C. § 1-306](#), Official Comment 1 (referring to [U.C.C. § 1-304](#)).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 348

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

1. Discharge Other Than by Payment

§ 348. Discharge of obligation to pay on negotiable instrument by cancellation or renunciation—Requirement of intentional act

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435, 438

A.L.R. Library

[Unintentional cancellation of negotiable instrument under U.C.C. Article 3, 59 A.L.R.4th 617](#)

Treatises and Practice Aids

As to intent to discharge and destruction of instrument, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

For a party to be discharged from liability on an instrument by cancellation or renunciation, the holder must intentionally cancel the instrument or renounce it.¹ Thus, liability is not extinguished by the act of unintentionally stamping the instrument "paid."² Moreover, cancellation or renunciation of a promissory note and release of security is ineffective if it is unintentional or procured by mistake, such as where note was payable to both lenders, and colender thus could not discharge or release interest of first lender in note without her consent.³ An accidental destruction of the instrument does not discharge the parties; in the case of an accidental destruction, the liabilities of the parties on the instrument remain unchanged.⁴ Likewise, a mistaken communication or other indication that a note has been paid which results from a clerical error will not discharge an

obligor from liability, since the requisite intent to cancel is lacking in such a case.⁵

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [SS Funding LLC v. Phelan](#), 981 So. 2d 1282 (Fla. 3d DCA 2008) (sufficient evidence supported the trial court's conclusion that a lender that sent promissory notes to a borrower intended to discharge the borrower of its obligations under the notes where the parties had entered into a memorandum of understanding (MOU) that combined the balance remaining on the notes with an additional loan into a new obligation of the borrower, the borrower began to make payments pursuant to the MOU and stopped making payments on the notes, the notes were returned to the borrower after the borrower sent a message asking that the notes be sent to its attorney to be cancelled, and there were no notations on the notes or correspondence indicating that the notes were to be held in escrow and not cancelled); [Gover v. Home and City Sav. Bank](#), 574 So. 2d 306, 13 U.C.C. Rep. Serv. 2d 1183 (Fla. 1st DCA 1991) (cancellation or renunciation is ineffective if it is unintentional or procured by mistake); [Credit Recoveries, Inc. v. Crow](#), 989 So. 2d 233 (La. Ct. App. 2d Cir. 2008) (debt evidenced by a note was tacitly remitted, such that the debt was cancelled, by the bank's return of the proffered note payments as overpayments, and the issuance of IRS Form 1099-C titled "Cancellation of Indebtedness").

² [Peoples Bank of South Carolina, Inc. v. Robinson](#), 272 S.C. 155, 249 S.E.2d 784, 25 U.C.C. Rep. Serv. 799 (1978); [Carter County Bank v. Craft Industries, Inc.](#), 639 S.W.2d 661, 34 U.C.C. Rep. Serv. 1632 (Tenn. Ct. App. 1982); [Manley v. Wachovia Small Business Capital](#), 349 S.W.3d 233 (Tex. App. Dallas 2011).

³ [All Real Estate Title Services, Inc. v. Minqh Quang Vu](#), 67 So. 3d 260 (Fla. 2d DCA 2010).

⁴ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-604:9 [Rev.] (3d ed.).

⁵ [FirsTier Bank, N.A. v. Triplett](#), 242 Neb. 614, 497 N.W.2d 339, 20 U.C.C. Rep. Serv. 2d 549 (1993); [G.E. Capital Mortg. Services, Inc. v. Neely](#), 135 N.C. App. 187, 519 S.E.2d 553, 39 U.C.C. Rep. Serv. 2d 1170 (1999); [Manley v. Wachovia Small Business Capital](#), 349 S.W.3d 233 (Tex. App. Dallas 2011).

11 Am. Jur. 2d Bills and Notes § 349

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

1. Discharge Other Than by Payment

§ 349. Discharge of obligation by acts which would discharge simple contract for payment of money

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435

If the person entitled to enforce an instrument does an act which would discharge the obligation of an obligor on a simple contract, the obligor on the instrument is discharged.¹ An obligation therefore may be discharged on grounds such as failure of consideration,² estoppel,³ duress,⁴ accord and satisfaction,⁵ or novation.⁶

As is true for monetary obligations governed by general contract law, the release of one or more, but less than all of the obligors on a negotiable instrument releases the other codebtors who are jointly and severally bound.⁷

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [§ 343.](#)

² *Berta v. Rocchio*, 149 Colo. 325, 369 P.2d 51 (1962); *Hunter v. McLelland*, 143 Ga. App. 746, 240 S.E.2d 153, 24 U.C.C. Rep. Serv. 172 (1977); *Tallahassee Bank & Trust Co. v. Raines*, 125 Ga. App. 263, 187 S.E.2d 320, 10 U.C.C. Rep. Serv. 665 (1972).

As to failure of consideration, generally, see [Am. Jur. 2d, Contracts §§ 635 to 637](#).

³ *Com. Bank & Trust Co. v. Plotkin*, 371 Mass. 218, 355 N.E.2d 917, 20 U.C.C. Rep. Serv. 692 (1976) (a debtor's detrimental reliance on a misrepresentation made by the creditor may give rise to a defense in the nature of an estoppel sufficient to discharge the obligor).

⁴ *Mancino v. Friedman*, 69 Ohio App. 2d 30, 23 Ohio Op. 3d 27, 429 N.E.2d 1181 (8th Dist. Cuyahoga County 1980). As to the invalidity of contracts obtained by duress, coercion, or undue influence, see [Am. Jur. 2d, Contracts §§ 212 to 214](#).

215.

⁵ As to accord and satisfaction by use of an instrument as payment, see § 356.

⁶ § 350.

⁷ *Wood v. Eminger*, 1940-NMSC-077, 44 N.M. 636, 107 P.2d 557 (1940) (stating that the reason for the rule is that the releasing creditor should not be allowed to enforce the obligation against one whose right of contribution has been destroyed by the release); *Economy Sav. & Loan Co. v. Weir*, 105 Ohio App. 531, 6 Ohio Op. 2d 254, 153 N.E.2d 155 (3d Dist. Marion County 1957); *Bede v. Tondre*, 86 R.I. 92, 134 A.2d 122 (1957).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 350

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

1. Discharge Other Than by Payment

§ 350. Discharge of obligation by acts which would discharge simple contract for payment of money—Renewal or novation

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  430, 435

A.L.R. Library

Renewal note signed by one comaker as discharge of nonsigning comakers, 43 A.L.R.3d 246

Trial Strategy

Novation of Contract by Substitution of Debtors, 9 Am. Jur. Proof of Facts 2d 159

Forms

Forms relating to note extinguishment or discharge, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code; Am. Jur. Pleading and Practice Forms, Novation [[Westlaw®\(r\) Search Query](#)]

The giving of a new note for a debt evidenced by a former note does not extinguish the old note unless such is the intention of the parties,¹ nor is there a presumption of the extinguishment of the original paper by the execution and delivery of a new note.² Indeed, as a general rule, the mere execution of a renewal note evidences the same debt by a new promise; it, therefore, does not constitute a payment or discharge of the original note, but operates only as an extension of time for payment.³ In order to constitute a discharge of an obligation by novation, there must be a mutual agreement by the creditor and debtor to extinguish the old obligation and substitute the new.⁴ Whether the execution of a note is a renewal of or payment for a previous note is a matter of intention of the parties,⁵ to be determined by analyzing the facts and circumstances surrounding the transaction.⁶

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

- ¹ [Inwood National Bank v. Wells Fargo Bank, N.A.](#), 463 S.W.3d 228, 86 U.C.C. Rep. Serv. 2d 483 (Tex. App. Dallas 2015).
- ² [Lissiak v. SW Loan OO, L.P.](#), 499 S.W.3d 481 (Tex. App. Tyler 2016).
- ³ [Marable v. First Union Nat. Bank](#), 232 Ga. App. 628, 502 S.E.2d 557 (1998) (a loan extension agreement did not alter a debtor's obligation to make scheduled monthly payments on a promissory note); [American Bank of St. Paul v. Coating Specialties, Inc.](#), 787 N.W.2d 202 (Minn. Ct. App. 2010).
As to the discharge of secondary obligors resulting from extensions, see §§ 373, 374.
As to the effect of a renewal note on the maturity of the obligation evidenced by an instrument, see § 173.
- ⁴ [Raico v. Concorde Funding Group](#), 60 A.D.3d 834, 875 N.Y.S.2d 251 (2d Dep't 2009); [Baccus v. Westgate Management Corp.](#), 981 S.W.2d 383 (Tex. App. San Antonio 1998) (the giving of a new note for a debt evidenced by a former note does not extinguish the old note unless the parties so intend).
The tender of subsequent note may, in some cases, operate as payment of original note, where the evidence indicates that this was parties' intent. [Paloian v. Grupo Serla S.A. de C.V.](#), 433 B.R. 19, 72 U.C.C. Rep. Serv. 2d 253 (N.D. Ill. 2010) (applying Illinois law).
As to an implied agreement to rescind or terminate a contract arising from the making or performance of a new contract, see [Am. Jur. 2d, Contracts](#) § 529.
- ⁵ [Fitch v. State](#), 851 So. 2d 103 (Ala. Crim. App. 2001); [Oil Field Gas Co. v. International Supply Co.](#), 1940 OK 250, 187 Okla. 262, 103 P.2d 91 (1940); [First Peoples Bank of Tennessee v. Hill](#), 340 S.W.3d 398 (Tenn. Ct. App. 2010).
- ⁶ [In re D & K Aviation, Inc.](#), 349 B.R. 169 (Bankr. S.D. Ohio 2006) (applying Ohio law).

11 Am. Jur. 2d Bills and Notes § 351

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 351. To whom payment made on obligation under negotiable instrument

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  427

Treatises and Practice Aids

As to [U.C.C. 3-602](#) [Rev] payment, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev]
Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to defense of note paid, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code
[[Westlaw®\(r\): Search Query](#)]

Article 3 of the Uniform Commercial Code¹ provides the rules governing payment obligations arising under a negotiable instrument, and it supplies the rules for identifying the proper party to whom a note's maker must make payment in order to satisfy and discharge the obligations under the note.²

Except as otherwise provided by statute,³ an instrument is paid to the extent payment is made by or on behalf of a party obliged to pay the instrument, and to a person entitled to enforce the instrument.⁴

In addition, except as otherwise provided by statute,⁵ a note is paid to the extent payment is made by or on behalf of a party obliged to pay the note to a person that formerly was entitled to enforce the note only, if at the time of the payment, the party obliged to pay has not received adequate notification that the note has been transferred and that payment is to be made to the transferee.⁶ A notification is adequate only if it:

- (1) is signed by the transferor or the transferee;
- (2) reasonably identifies the transferred note; and
- (3) provides an address at which payments subsequently are to be made.⁷

Definition:

As used in this section, “signed,” with respect to a record that is not a writing, includes the attachment to or logical association with the record of an electronic symbol, sound, or process with the present intent to adopt or accept the record.⁸

Comments:

One subsection of U.C.C. Article 3, Part 6 on discharge and payment of negotiable instruments covers payments made in a traditional manner, to the person entitled to enforce the instrument.⁹ Another subsection, which provides an alternative method of payment,¹⁰ deals with the situation in which a person entitled to enforce the instrument transfers the instrument without giving notice to parties obligated to pay the instrument. If that happens and one of those parties subsequently makes a payment to the transferor, the payment is effective even though it is not made to the person entitled to enforce the instrument.¹¹

In determining the party to whom a payment is made, courts should look to traditional rules of agency. Thus, if the original payee of a note transfers ownership of the note to a third party but continues to service the obligation, the law of agency might treat payments made to the original payee as payments made to the third party.¹²

Subject to the exceptions to the rule that discharge may be made by payment,¹³ to the extent of a payment under the subsections discussed above,¹⁴ the obligation of the party obliged to pay the instrument is discharged even though payment is made with knowledge of a claim to the instrument.¹⁵

Upon request, a transferee must seasonably furnish reasonable proof that the note has been transferred, and, unless the transferee complies with the request, a payment to the person that formerly was entitled to enforce the note is effective even if the party obliged to pay the note has received proper notification.¹⁶ Checks that are signed without a payee are payable to the bearer and, thus, are enforceable by any person in possession of the checks.¹⁷

Subject to the exceptions to the rule that discharge may be made by payment,¹⁸ a transferee, or any party that has acquired rights in the instrument directly or indirectly from a transferee, including any such party that has rights as a holder in due course, is deemed to have notice of any payment that is made under the provision pertaining to payment subject to notification of transfer¹⁹ after the date that the note is transferred to the transferee but before the party obliged to pay the note receives adequate notification of the transfer.²⁰

Footnotes

¹ U.C.C. §§ 3-101 to 3-605.

² *In re Stanley*, 514 B.R. 27 (Bankr. D. Nev. 2012) (applying Nevada law).

³ U.C.C. § 3-602(e) (2002 Rev.).

⁴ U.C.C. § 3-602(a) (2002 Rev.).

If a borrower pays a person entitled to enforce the note, the borrower's obligations are discharged to the extent of the amount paid. *In re Walker*, 466 B.R. 271, 76 U.C.C. Rep. Serv. 2d 818 (Bankr. E.D. Pa. 2012) (applying Pennsylvania law).

Because payment to one nonalternative copayee without the endorsement of the other is not payment to a holder, it does not discharge the drawer of either liability on the instrument or the underlying obligation. *McAllen Hospitals, L.P. v. State Farm County Mut. Ins. Co. of Texas*, 433 S.W.3d 535, 83 U.C.C. Rep. Serv. 2d 683 (Tex. 2014); *ViewPoint Bank v. Allied Property and Cas. Ins. Co.*, 439 S.W.3d 626, 84 U.C.C. Rep. Serv. 2d 295 (Tex. App. Dallas 2014), also discussed in § 344.

While negotiation of a promissory note is complete only on the transfer of physical possession thereof, possession alone does not establish that the party in possession is a "holder" of the note, with a right to receive payments thereon. *In re Wells*, 407 B.R. 873, 69 U.C.C. Rep. Serv. 2d 382 (Bankr. N.D. Ohio 2009) (applying Ohio law).

Payment to an authorized agent is deemed to be payment to a holder in possession of the negotiable instrument. *Citywide Banks v. Armijo*, 313 P.3d 647, 75 U.C.C. Rep. Serv. 2d 789 (Colo. App. 2011); *Gusma Properties, L.P. v. Travelers Lloyds Insurance Company*, 514 S.W.3d 319, 91 U.C.C. Rep. Serv. 2d 604 (Tex. App. Houston 14th Dist. 2016).

Payment of an instrument to a collecting bank is the equivalent of payment to its principal, the owner of the instrument, and constitutes an absolute discharge thereof. *Jackson v. Pride Oil & Gas Properties, Inc.*, 104 So. 3d 6 (La. Ct. App. 2d Cir. 2012), writ denied, 104 So. 3d 444 (La. 2012).

The holder of an outdated certificate of deposit (CD) who brought an action against a bank demanding payment of principal and interest failed to establish that the CD was not paid to a person entitled to enforce the instrument, where the holder found the CD in a storage facility and had no evidence concerning whether it was presented for payment by a previous holder. *Griffith v. Mellon Bank, N.A.*, 328 F. Supp. 2d 536, 54 U.C.C. Rep. Serv. 2d 373 (E.D. Pa. 2004), decision aff'd, 173 Fed. Appx. 131, 59 U.C.C. Rep. Serv. 2d 135 (3d Cir. 2006) (applying Pennsylvania law).

The lack of an endorsement on a promissory note did not deprive the party holding the note of the right to enforce it, but merely stripped the party of its presumed right to payment and required it to prove the transaction by which it acquired the instrument. *In re Carlyle*, 242 B.R. 881, 43 U.C.C. Rep. Serv. 2d 905 (Bankr. E.D. Va. 1999) (applying Virginia law).

As to the place of payment where the instrument does not specify, see § 103.

As to exceptions to discharge by payment, see §§ 353, 354.

⁵ U.C.C. § 3-602(e) (2002 Rev.).

⁶ U.C.C. § 3-602(b) (2002 Rev.).

⁷ U.C.C. § 3-602(b) (2002 Rev.).

⁸ U.C.C. § 3-602(f) (2002 Rev.).

⁹ U.C.C. § 3-602(a) (2002 Rev.).

¹⁰ U.C.C. § 3-602(b) (2002 Rev.).

¹¹ U.C.C. § 3-602 (2002 Rev.), Official Comment 2.

¹² U.C.C. § 3-602 (2002 Rev.), Official Comment 3.

As to an agent's authority to receive payment, see Am. Jur. 2d, Agency §§ 125 to 137.

¹³ U.C.C. § 3-602(e) (2002 Rev.).

¹⁴ U.C.C. § 3-602(a), (b).

15 [U.C.C. § 3-602\(c\)](#) (2002 Rev).

As to payment with knowledge of adverse claim, see [§ 354](#).

16 [U.C.C. § 3-602\(b\)](#) (2002 Rev).

17 [In re Hussain, 508 B.R. 417 \(B.A.P. 9th Cir. 2014\)](#) (applying California law).

18 [U.C.C. § 3-602\(e\)](#) (2002 Rev).

19 [U.C.C. § 3-602\(b\)](#) (2002 Rev).

20 [U.C.C. § 3-602\(d\)](#) (2002 Rev).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 352

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 352. Medium of payment used to discharge obligation or note

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  430 to 432

Forms

Forms relating to note discharged by rendition of services, see Am. Jur. Pleading and Practice Forms, Commercial Code
[Westlaw®(r) Search Query]

As a general rule, payment of promissory notes must be made in money.¹ Thus, the holder of a note cannot be required to accept a deed to real estate securing a note as full satisfaction of the note.² Since a check is not included in the Uniform Commercial Code definition of "money,"³ payment by check does not discharge a debt unless and until the check is honored.⁴ Thus, a creditor has a right to refuse a debtor's check given in part payment of a note, at least where the check is not guaranteed by the bank on which it is drawn.⁵

Notwithstanding the general rule that payment must be made in money, the parties may agree on a mode of satisfying an obligation other than by the payment of money, such as by the cancellation of mutual indebtedness,⁶ or by the furnishing of shares of common stock,⁷ services or commodities.⁸ However, where the payee of a promissory note agrees to accept payment in the form of an equity interest in a restaurant, but does not receive evidence of an ownership interest within a reasonable time, there is no payment to the payee and no discharge of liability on the note.⁹

Footnotes

¹ [Green Acres Enterprises, Inc. v. Freeman](#), 876 S.W.2d 636 (Mo. Ct. App. W.D. 1994).

² [American Mini-Storage, Marietta Blvd., Ltd. v. Investguard, Ltd.](#), 196 Ga. App. 862, 397 S.E.2d 199 (1990).

³ U.C.C. § 1-201(b)(24) (2002 Rev.).

⁴ [Aztec Gas & Oil Corp. v. Roemer Oil Co.](#), 948 P.2d 902, 36 U.C.C. Rep. Serv. 2d 799 (Wyo. 1997). As to the taking of an instrument as payment, see § 116.

⁵ [Midwest Federal Sav. and Loan Ass'n of Minot v. Kouba](#), 335 N.W.2d 780, 40 A.L.R.4th 338 (N.D. 1983).

The payee's acceptance of checks for 46 monthly payments evidenced a course of dealing which showed that payment by personal check was an approved manner of making payments. [Neuman v. Ferris](#), 432 So. 2d 641 (Fla. 4th DCA 1983).

The fact that a creditor accepted a check for part of a debt and a note signed by a third party for the balance did not discharge the liability of the debtor in the absence of any agreement that the debtor was to be discharged. [Griffiths v. Phenix Supply Co., Inc.](#), 192 Ga. App. 651, 385 S.E.2d 789 (1989).

⁶ [Gibson v. Harl](#), 857 S.W.2d 260 (Mo. Ct. App. W.D. 1993) (the makers of a note were discharged from liability by their exercise of the right to set off the obligation against an obligation the payees of the note owed to them under a lease).

A former mother-in-law was adequately repaid for a loan, memorialized by a promissory note, made to her son and former daughter-in-law for the down payment on a house through the former daughter-in-law's quitclaim deed and a divorce decree; loan amount was preserved as equity by the divorce decree and the quitclaim by former daughter-in-law of her one-quarter interest in the home to former mother-in-law and former husband. [Yurevich v. Williams](#), 302 Ga. App. 162, 690 S.E.2d 476 (2010).

As to cancellation of mutual debts, generally, see [Am. Jur. 2d, Payment](#) § 17.

⁷ [TrueStar Petroleum Corp. v. Eagle Oil & Gas Co.](#), 323 S.W.3d 316 (Tex. App. Dallas 2010) (holding that that maker's failure to strictly comply with the terms of the note's provision allowing the maker, at its option at maturity, to pay all or part of principal amount in shares of its common stock required maker to pay balance of note in cash on maturity date).

⁸ [Beaumont Implement Co. v. Clubb](#), 140 S.W.2d 212 (Tex. Civ. App. Beaumont 1940).

⁹ [Lutz v. Gatlin](#), 22 Wash. App. 424, 590 P.2d 359, 26 U.C.C. Rep. Serv. 129 (Div. 3 1979).

11 Am. Jur. 2d Bills and Notes § 353

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 353. Exceptions to discharge of obligation or note by payment

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  427

Treatises and Practice Aids

As to exceptions to discharge under [U.C.C. 3-602](#) [Rev], see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

The obligation of a party to pay the instrument is not discharged if the person making payment knows that the instrument is a stolen instrument and pays a person it knows is in wrongful possession of the instrument.¹ To call this exception into operation, it is necessary that the person making payment have actual knowledge of the facts designated by statute; reason to know, suspicion, or notice is not sufficient.² This requires knowledge both as to the prior history of the instrument and the character of the possession of the person claiming payment. Thus, the mere fact that the person making payment knew that it had been stolen at some earlier time is insufficient to make the exception applicable.³

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-602\(e\)\(2\)](#) (2002 Rev).

² [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-602:14 \[Rev.\] \(3d ed.\)](#).

3

[Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-602:14 \[Rev.\] \(3d ed.\).](#)

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 354

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 354. Exceptions to discharge of obligation or note by payment—Payment with knowledge of adverse claim

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  427

Treatises and Practice Aids

As to adverse claim to instrument: injunction against payment, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to adverse claimants, and injunctions against payment, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\) Search Query](#)]

The obligation of a party to pay an instrument is not discharged if a claim to the instrument, as defined by statute,¹ is enforceable against the party receiving payment and either:

- (1) payment is made with knowledge by the payor that payment is prohibited by injunction or similar process of a court of competent jurisdiction; or

(2) in the case of an instrument other than a cashier's check, teller's check, or certified check, the party making payment has accepted indemnity from the person having a claim to the instrument against loss resulting from refusal to pay the person entitled to enforce the instrument.²

Comment:

The phrase "claim to the instrument" means a claim of ownership or possession and not a claim in recoupment.³

The obligor has no obligation to accept an offer of indemnity and may refuse the offer of indemnity and obtain a discharge by his or her payment unless the claimant obtains an injunction against payment and the obligor has knowledge of that injunction.⁴

Observation:

It is not necessary, under the foregoing statutory provision, that the court order prohibiting payment be called an injunction; any payment-prohibiting order or decree issued by a court of competent jurisdiction satisfies the requirements of the statute.⁵

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-306 (2002 Rev).

² U.C.C. § 3-602(e)(1) (2002 Rev).

³ U.C.C. § 3-602 (2002 Rev), Official Comment 1.

⁴ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-602:12 [Rev.] (3d ed.).

⁵ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-602:11 [Rev.] (3d ed.).

11 Am. Jur. 2d Bills and Notes § 355

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 355. Effect of tender of payment on obligation or note; prepayments

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  428 to 432

Treatises and Practice Aids

As to tender of payment, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to tender, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\) Search Query](#)]

If tender of payment of an obligation to pay an instrument is made to a person entitled to enforce the instrument, the effect of tender is governed by the principles of law applicable to tender of payment under a simple contract.¹ Tender may also be made to a person authorized to receive payment on behalf of the person entitled to enforce the instrument.²

A party may not be excused from its obligation on a note under the tender of payment doctrine when tender is made before the note is due, unless the loan agreement provides the borrower with a right to prepay the loan.³ Furthermore, even an

absolute prohibition against prepayment will not be invalidated as unduly restrictive, because a lender's interest in guaranteeing a certain net return by loaning money at a particular interest rate for a specific length of time is entirely legitimate.⁴

Definitions:

A "prepayment penalty" fee or premium in a note serves a valid purpose in compensating for the anticipated interest a lender will not receive if a loan is paid off prematurely, and in compensating the lender for payments no longer being made in regular installments.⁵ A "make-whole premium" is a contractual substitute for interest lost on promissory notes redeemed before their expected due date, and is meant to ensure that the lender is compensated, if paid earlier than the original maturity of loan, for the interest that it will not receive.⁶

If a lender does not waive the right to refuse early payment, a borrower may not prepay the note without paying all future interest as well;⁷ if a lender does expressly waive the right to refuse early payment, then it is not entitled to any prepayment penalty unless the contract expressly provides for such prepayment penalty.⁸

A lender typically loses its right to a premium when it elects to accelerate the debt, because acceleration advances the maturity date and, by definition, the note cannot be prepaid;⁹ although parties to loan agreements may agree that prepayment premiums are due even after debt acceleration.¹⁰

It has been held that noteholders, who would otherwise be entitled to a make-whole premium by prepayment, are not entitled to such make-whole premium after automatic acceleration of the debt due to the debtors' bankruptcy filing, because in such a case, prepayment of notes is not a voluntary early "redemption" of notes prior to their due date.¹¹ However, it has also been held that the mere fact that promissory notes had been automatically accelerated as result of debtor-borrower's Chapter 11 filing, pursuant to one provision of trust indenture, does not render another provision requiring payment of an early redemption premium inapplicable; the provisions must be construed together in order to give effect to both.¹²

If tender is made, the obligation of the obligor to pay interest after the due date on the amount tendered is discharged.¹³ Similarly, a judgment debtor may halt the accrual of interest on a judgment by tendering payment of the judgment, costs, and interest accrued.¹⁴ However, a tender that is conditional does not stop the running of interest on the offeror's obligation to the offeree.¹⁵

If presentment is required with respect to an instrument, and the obligor is able and ready to pay on the due date at every place of payment stated in the instrument, the obligor is deemed to have made tender of payment on the due date to the person entitled to enforce the instrument.¹⁶ When the obligor is sued for interest, the obligor will have the burden of proving that it meets the conditions specified above so that interest will stop running on the date of the constructive tender.¹⁷

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-603(a) (2002 Rev.).
A tender must include everything to which the creditor is entitled, and tender of any less sum is nugatory and ineffective as a tender. *Telemark Development Group, Inc. v. Mengelt*, 313 F.3d 972, 49 U.C.C. Rep. Serv. 2d 880 (7th Cir. 2002) (applying Illinois law).

The holder of a note did not have actual knowledge of debtors' purported tender of payment, and thus tender of third party checks did not constitute payment where the only identifying information on the checks was debtors' related bankruptcy case number on the memo line of the checks. *U.S. Bank Nat. Ass'n v. Whitney*, 119 Wash. App. 339, 81 P.3d 135, 52 U.C.C. Rep. Serv. 2d 1 (Div. 3 2003).

2 Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-603:5 [Rev.] (3d ed.).

3 Federal Financial Co. v. Delgado, 1 S.W.3d 181, 40 U.C.C. Rep. Serv. 2d 759 (Tex. App. Corpus Christi 1999).

4 George v. Fowler, 96 Wash. App. 187, 978 P.2d 565 (Div. 1 1999).

A borrower does not have the right to prepay an instrument in the absence of a prepayment clause since prepayment affects the lender's bargained-for right to a stream of income over a fixed period of time. *In re Solutia Inc.*, 379 B.R. 473 (Bankr. S.D. N.Y. 2007) (applying New York law).

5 Planned Pethood Plus, Inc. v. KeyCorp, Inc., 228 P.3d 262 (Colo. App. 2010).

6 Matter of MPM Silicones, L.L.C., 874 F.3d 787 (2d Cir. 2017), cert. denied, 138 S. Ct. 2653, 201 L. Ed. 2d 1051 (2018) and cert. denied, 138 S. Ct. 2653, 201 L. Ed. 2d 1051 (2018); *In re MPM Silicones, L.L.C.*, 596 B.R. 416 (S.D. N.Y. 2019).

The purpose of a promissory note's make-whole provision is to compensate the lender for lost interest. *In re Ultra Petroleum Corporation*, 913 F.3d 533 (5th Cir. 2019).

7 In re Denver Merchandise Mart, Inc., 740 F.3d 1052 (5th Cir. 2014) (applying Colorado law).

8 In re Denver Merchandise Mart, Inc., 740 F.3d 1052 (5th Cir. 2014) (applying Colorado law); *Kirk v. Kitchens*, 49 P.3d 1189 (Colo. App. 2002).

The lender is entitled to charge a penalty to the borrower for the privilege of prepayment. *Norwest Bank Minnesota v. Blair Road Associates, L.P.*, 252 F. Supp. 2d 86 (D.N.J. 2003) (applying New Jersey law).

9 In re Madison 92nd Street Associates LLC, 472 B.R. 189 (Bankr. S.D. N.Y. 2012) (applying New York law).

10 In re AE Hotel Venture, 321 B.R. 209 (Bankr. N.D. Ill. 2005).

As to the effect of an acceleration clause, see §§ 93, 93, 164 to 167.

11 Matter of MPM Silicones, L.L.C., 874 F.3d 787 (2d Cir. 2017), cert. denied, 138 S. Ct. 2653, 201 L. Ed. 2d 1051 (2018) and cert. denied, 138 S. Ct. 2653, 201 L. Ed. 2d 1051 (2018).

12 In re Energy Future Holdings Corp., 842 F.3d 247 (3d Cir. 2016) (applying New York law).

13 U.C.C. § 3-603(c) (2002 Rev).

14 Browning, Ektelon Div. v. Williams, 348 Ill. App. 3d 830, 283 Ill. Dec. 143, 807 N.E.2d 984 (1st Dist. 2004).

15 Buffalo Ridge Corp. v. Lamar Advertising of South Dakota, Inc., 2011 SD 4, 793 N.W.2d 809 (S.D. 2011).

16 U.C.C. § 3-603(c) (2002 Rev).

17 Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-603:6 [Rev.] (3d ed.).

11 Am. Jur. 2d Bills and Notes § 356

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 356. Accord and satisfaction by use of instrument

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435

A.L.R. Library

Modern status of rule that acceptance of check purporting to be final settlement of disputed amount constitutes accord and satisfaction, 42 A.L.R.4th 12

Treatises and Practice Aids

As to accord and satisfaction by use of instrument, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to accord and satisfaction, payment by check, see Am. Jur. Pleading and Practice Forms, Accord and

Satisfaction [Westlaw®(r) Search Query]

If a person against whom a claim is asserted proves that (1) he or she, in good faith, tendered an instrument to the claimant as full satisfaction of the claim; (2) the amount of the claim was unliquidated or subject to a bona fide dispute; and (3) the claimant obtained payment of the instrument, various rules determine whether or not an accord and satisfaction by use of an instrument has occurred.¹

Good faith is demonstrated when the party tendering the instrument offers a check with the intent to honestly enter into an accord and satisfaction while observing reasonable commercial standards of fair dealing.² The focus of the good faith inquiry, is on the offer of the accord and not on the actions of the parties in performing the underlying contract.³

Comment:

The provision of the Uniform Commercial Code pertaining to accord and satisfaction by use of instrument does not apply to cases in which the debt is a liquidated amount and not subject to a bona fide dispute.⁴

Unless otherwise specified,⁵ the claim is discharged if the person against whom the claim is asserted proves that the instrument or an accompanying written communication contained a conspicuous statement to the effect that the instrument was tendered as full satisfaction of the claim.⁶ The statutory requirement of a conspicuous statement, to the effect that the instrument is tendered as full satisfaction of a claim, necessarily contemplates that no specific language is required for an accord and that each case must be considered on its own merits.⁷ Where a debtor offers an amount less than that demanded and denies the remainder, and a reasonable person would have understood the offer to be tendered as full satisfaction of the disputed claim, the claim is discharged when the claimant accepts and negotiates the instrument in payment for the lesser sum.⁸

A claim is discharged if the person against whom the claim is asserted proves that, within a reasonable time before collection of the instrument was initiated, the claimant or an agent of the claimant having direct responsibility with respect to the disputed obligation knew that the instrument was tendered in full satisfaction of the claim.⁹ Where a debtor seeks to establish an accord and satisfaction by virtue of the foregoing provision, on the basis of the knowledge of the creditor or its agent, the debtor has the burden of proving that all of the statutory requirements are met.¹⁰

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-311(a).

As to the use of an instrument as payment, generally, see § 116.

² *Webb Business Promotions, Inc. v. American Electronics & Entertainment Corp.*, 617 N.W.2d 67, 42 U.C.C. Rep. Serv. 2d 534 (Minn. 2000).

³ *Ex parte Meztista*, 845 So. 2d 795, 51 U.C.C. Rep. Serv. 2d 461 (Ala. 2001); *Webb Business Promotions, Inc. v. American Electronics & Entertainment Corp.*, 617 N.W.2d 67, 42 U.C.C. Rep. Serv. 2d 534 (Minn. 2000).

⁴ U.C.C. § 3-311, Official Comment 4.

5 U.C.C. § 3-311(c).

6 U.C.C. § 3-311(b).

7 Brucato v. Ezenia! Inc., 351 F. Supp. 2d 464, 55 U.C.C. Rep. Serv. 2d 718 (E.D. Va. 2004) (applying Virginia law).

8 Brucato v. Ezenia! Inc., 351 F. Supp. 2d 464, 55 U.C.C. Rep. Serv. 2d 718 (E.D. Va. 2004) (applying Virginia law).

9 U.C.C. § 3-311(d).

10 Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-311:19 [Rev.] (3d ed.).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 357

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 357. Accord and satisfaction by use of instrument—Organizational claimant

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435

Except as otherwise provided in the Uniform Commercial Code,¹ a claim is not discharged if either of the following applies:

- (1) the claimant, if an organization, proves that within a reasonable time before the tender it sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including any instrument tendered as full satisfaction of a debt, were to be sent to a designated person, office, or place, and further proves that the instrument or accompanying communication in question were not received by the designated person, office, or place;² or
- (2) the claimant, including any organization which has not sent a statement of the type allowed by the preceding paragraph, proves that within 90 days after payment of the instrument, the claimant tendered repayment of the amount of the instrument to the person against whom the claim is asserted.³

Comment:

The foregoing provision of the U.C.C. is intended to protect an organizational claimant against an inadvertent accord and satisfaction, which could otherwise occur if payments are received and processed by employees of the organization other than those concerned with disputed claims.⁴

Footnotes

¹ U.C.C. § 3-311(d).

² U.C.C. § 3-311(c)(1).

³ U.C.C. § 3-311(c)(2).

A contractor's scribbled notes to the effect that the check he received from the debtor-landowners as a "final payment" of all claims between the parties was not, in fact, a full payment of his claim did not nullify his acceptance of the check in cashing it, and did not prevent the check from operating as an accord and satisfaction, where the contractor failed to return the debtors' payment in the 90-day period specified by statute. *In re Runge*, 226 B.R. 298, 36 U.C.C. Rep. Serv. 2d 1097 (Bankr. D. N.H. 1998) (applying New Hampshire law).

⁴ U.C.C. § 3-311, Official Comment 5.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 358

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 358. Accord and satisfaction by use of instrument—Effect of acceptance of payment under reservation of rights

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435

Treatises and Practice Aids

As to form of reservation—explicit reservation required, see Lawrence's Anderson on the Uniform Commercial Code, Article 1 [Rev] General Provisions [[Westlaw®\(r\): Search Query](#)]

A party who assents, with an explicit reservation of rights, to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved; words such as “without prejudice,” “under protest,” or the like are sufficient to reserve all rights.¹ However, the foregoing provision of the Uniform Commercial Code allowing a reservation of rights does not alter the law of accord and satisfaction,² and the section of the U.C.C. concerning accord and satisfaction by use of an instrument³ governs full satisfaction checks.⁴

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹

[U.C.C. § 1-308\(a\).](#)

As to performance or acceptance under reservation of rights, see [Am. Jur. 2d, Commercial Code § 32](#).

² U.C.C. § 1-308(b).

A check issued by a buyer of goods to a seller for less than the full amount due, which contained a “settlement in full” notation made by the buyer, created a binding accord and satisfaction when the seller indorsed and deposited the check, despite the seller’s express “reservation of rights” notation on the check. *Stultz Elec. Works v. Marine Hydraulic Engineering Co.*, 484 A.2d 1008, 39 U.C.C. Rep. Serv. 1186 (Me. 1984).

³ U.C.C. § 3-311.

⁴ U.C.C. § 3-311, Official Comment 3.

Where a contractor offers payment conditioned upon a subcontractor’s assent to that payment being in full satisfaction of the contractor’s obligation, the subcontractor cannot reject the condition by unilaterally noting on the check a reservation of rights to collect the remaining balance prior to negotiating the instrument; by cashing the check, the subcontractor assents to the stated condition and accepts the proceeds of the check by virtue of the accord and satisfaction which thus results. *McKee Const. Co. v. Stanley Plumbing & Heating Co.*, 828 S.W.2d 700, 18 U.C.C. Rep. Serv. 2d 16 (Mo. Ct. App. S.D. 1992).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 359

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

a. In General

§ 359. Effect of judgment on negotiable instrument

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  435

The rule that a judgment merges the cause of action on which the suit resulting in the judgment was brought applies generally to judgments on negotiable instruments,¹ and subsequent suits on the instrument are barred.² However, the doctrine of merger by judgment, as applied to promissory notes relates only to such parties as are jointly liable thereon or to cases where a judgment is rendered against both the maker and any secondarily liable parties; thus, the fact that the creditor obtains a judgment against the maker of a note alone does not discharge an indorser if the judgment is not satisfied.³

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [In re Miller's Estate](#), 189 Or. 246, 218 P.2d 966 (1950).

² [Fish Meal Co. v. Brondum](#), 242 Miss. 573, 135 So. 2d 825 (1961); [Hawkins v. Wiest](#), 167 Mo. App. 439, 151 S.W. 789 (1912).

³ [Cline v. Receiver of Commercial Nat. Bank of Chatsworth](#), 90 F.2d 968 (C.C.A. 7th Cir. 1937); [Petri v. Manny](#), 99 Wash. 601, 170 P. 127, 1 A.L.R. 1595 (1918).

11 Am. Jur. 2d Bills and Notes § 360

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(1) In General

§ 360. Finality of payment on draft or instrument; mistake as basis for recovery

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  434

A.L.R. Library

What constitutes change of position by payee so as to preclude recovery of payment made under mistake, 40 A.L.R.2d 997

Treatises and Practice Aids

As to relief from mistake, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

If the drawee of a draft pays or accepts the draft in the mistaken belief: (1) that payment of the draft had not been stopped, as allowed by statute;¹ or (2) that the signature of the drawer of the draft was authorized, the drawee may recover the amount of the draft from the person to whom or for whose benefit payment was made.² The right of a drawee to recover improper payments for such reasons is not affected by the failure of the drawee to exercise ordinary care in paying or accepting the

draft.³ However, the remedies available in the case of a payment by mistake may not be asserted against a person who took the instrument in good faith and for value or who, in good faith, changed position in reliance on the payment.⁴ Good faith relates to the state of mind of an individual seeking payment on a check.⁵

If an instrument has been paid by mistake and the case does not come within either of the two situations specified by statute,⁶ the person paying, may, to the extent permitted by the law governing mistake and restitution, recover the payment from the person to whom or for whose benefit payment was made.⁷

Comments:

Perhaps the most important class of cases that falls under the foregoing provision is that of payment by the drawee bank of a check with respect to which the bank has no duty to the drawer to pay, either because the drawer has no account with the bank or because available funds in the drawer's account are insufficient to cover the amount of the check.⁸

Restitution is allowed in the two most common cases in which the problem is presented: (1) payment of forged checks, and (2) checks on which the drawer has stopped payment. If the drawee acted under a mistaken belief that the check was not forged or had not been stopped, the drawee is entitled to recover the funds paid whether or not the drawee acted negligently. But in each case, the drawee loses the remedy if the person receiving payment was a person who took the check in good faith and for value or who in good faith changed position in reliance on the payment.⁹

Observations:

Under the common law, while money paid under a mistake of fact may be recovered, money paid due to a mistake of law, generally, is not recoverable.¹⁰

The right of a bank to recover a mistaken payment is not affected by the fact that the drawee retains the check in question beyond its midnight deadline.¹¹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 4-403 (2002 Rev).

² U.C.C. § 3-418(a) (2002 Rev).
As to the revocation of acceptance of a draft, see §§ 341, 342.

³ U.C.C. § 3-418(a) (2002 Rev).

⁴ U.C.C. § 3-418(c) (2002 Rev), further providing that this does not limit remedies provided by U.C.C. § 3-417 (2002 Rev) (presentment warranties) or U.C.C. § 4-407 (2002 Rev) (payor bank's right to subrogation on improper payment).

A bank that mistakenly issued a cashier's check in exchange for a personal check upon which a stop payment order had been placed had no remedy against the payee, where the payee took the personal check for value and acted in good

faith, because of its lack of knowledge of the stop payment order. [Flatiron Linen, Inc. v. First American State Bank](#), 23 P.3d 1209, 44 U.C.C. Rep. Serv. 2d 673 (Colo. 2001).

As to presentment warranties, see §§ [457](#) to [467](#).

As to a payor bank's right to subrogation on improper payment, see [Am. Jur. 2d, Banks and Financial Institutions](#) § [950](#).

⁵ [Flatiron Linen, Inc. v. First American State Bank](#), 23 P.3d 1209, 44 U.C.C. Rep. Serv. 2d 673 (Colo. 2001).

⁶ U.C.C. § [3-418\(a\)](#) (2002 Rev).

⁷ U.C.C. § [3-418\(b\)](#) (2002 Rev).

⁸ U.C.C. § [3-418](#) (2002 Rev), Official Comment 3.

⁹ U.C.C. § [3-418](#) (2002 Rev), Official Comment 1.

¹⁰ [Home Ins. Co. v. Honaker](#), 480 A.2d 652 (Del. 1984); [Kerr S.S. Co. v. Chicago Title & Trust Co.](#), 120 Ill. App. 3d 998, 76 Ill. Dec. 355, 458 N.E.2d 1009 (1st Dist. 1983).

¹¹ [First Nat. Bank in Harvey v. Colonial Bank](#), 898 F. Supp. 1220, 28 U.C.C. Rep. Serv. 2d 290 (N.D. Ill. 1995).

11 Am. Jur. 2d Bills and Notes § 361

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(1) In General

§ 361. Finality of payment on draft or instrument; mistake as basis for recovery—Effect of recovery for mistake

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  434

Treatises and Practice Aids

As to effect of recovery or revocation, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

If an instrument is paid by mistake and the payor recovers the payment, the instrument is deemed not to have been paid and is treated as dishonored.¹ The person from whom payment is recovered has rights as a person entitled to enforce the dishonored instrument.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-418\(d\)](#) (2002 Rev).

As to notice of dishonor of instruments, see §§ [317](#) to [328](#).

² [U.C.C. § 3-418\(d\)](#) (2002 Rev).
As to dishonor in general, see §§ [308](#) to [316](#).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 362

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(1) In General

§ 362. Recovery of payment on draft or instrument by drawee

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  434

Treatises and Practice Aids

As to the relation to Article 4, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

The right of the drawee to recover a payment after mistakenly paying or accepting the draft¹ is not affected by the rules under the Uniform Commercial Code article governing bank deposits and collections² that determine when an item is paid.³ Thus, even though a payor bank may have paid an item under the bank deposits and collections article,⁴ it may have a right to recover the payment under the code section⁵ governing payment or acceptance of a draft by mistake.⁶

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [§ 361.](#)

² U.C.C. §§ 4-101 to 4-111.

³ U.C.C. § 3-418 (2002 Rev), Official Comment 4.

⁴ U.C.C. § 4-215.

⁵ U.C.C. § 3-418 (2002 Rev).

⁶ U.C.C. § 3-418 (2002 Rev), Official Comment 4.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 363

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(1) In General

§ 363. Recovery of payment on draft or instrument for duress, fraud, or failure of consideration

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  434

A.L.R. Library

Economic duress or business compulsion in execution of promissory note, 79 A.L.R.3d 598

Trial Strategy

[Promissory Note Executed under Economic Duress or Business Compulsion, 11 Am. Jur. Proof of Facts 2d 23](#) §§ 14 to 27
(Proof that promissory note was executed under economic duress or business compulsion)

Payments made as a result of duress, fraud, mistake, or failure of consideration, generally, may be recovered.¹ This rule pertains as well in situations in which money has wrongfully been paid on a negotiable instrument.²

Observation:

Recovery of money wrongfully paid may be sought in an action for restitution³ or in an action for money had and received.⁴

The rule permitting recovery of money obtained through fraud, imposition, extortion, or undue advantage does not permit a recovery of the amount paid by a bank upon its customer's checks under a mistaken belief that the customer's account contained sufficient funds to cover the checks, where no fraud is charged and no misrepresentation or overreaching is shown.⁵

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ Am. Jur. 2d, Restitution and Implied Contracts § 90.
As to recovery of payments made by mistake, see §§ 360, 361.

² Maddox v. First Westroads Bank, 199 Neb. 81, 256 N.W.2d 647, 22 U.C.C. Rep. Serv. 743 (1977).

³ In re Men's Sportswear, Inc., 834 F.2d 1134 (2d Cir. 1987).

⁴ Central Bank & Trust Co. v. General Finance Corp., 297 F.2d 126 (5th Cir. 1961); Penalosa Co-op. Exchange v. A.S. Polonyi Co., 745 F. Supp. 580 (W.D. Mo. 1990).

⁵ Central Bank & Trust Co. v. General Finance Corp., 297 F.2d 126 (5th Cir. 1961).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 364

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(2) Where Signature is Forged or Unauthorized

§ 364. Recovery on instrument where drawer's signature forged or unauthorized; doctrine of *Price v. Neal*

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  434

The rule of *Price v. Neal*,¹ states that a drawee who accepts or pays an instrument on which the signature of the drawer is forged is bound on its acceptance and cannot recover back its payment. The rationale for this is that it is highly desirable to end the transaction on an instrument when it is paid rather than reopen and upset a series of commercial transactions at a later date when the forgery is discovered.²

The U.C.C. adopted the rule of *Price v. Neal* in its old finality of payment rule³ and in the current provisions governing payment or acceptance by mistake.⁴ The first of those provisions⁵ permits recovery of a payment where the drawee is under a belief that the drawer's signature is authorized, but the second relevant provision⁶ limits recovery by providing that it is not permitted against one who took the instrument in good faith and for value or who, in good faith, changed position in reliance on the payment.⁷ Thus, a drawee bank is usually liable to its checking account customer for payment of a check on which the customer's signature has been forged.⁸

Where a state diverges from the Uniform Commercial Code, in that its conception of good faith is a subjective standard, defined simply as "honesty in fact in the conduct or transaction concerned," rather than the observance of reasonable commercial standards of fair dealing, the final payment rule bars a drawer's claim that depository bank improperly permitted the drawer's employees to deposit purportedly forged checks in their personal accounts, where the bank understands the employees to be personally borrowing money in efforts to keep the drawer solvent, and believes that payments from the drawer to the employees are in repayment for those loans.⁹

CUMULATIVE SUPPLEMENT

Cases:

Article 3 of the Uniform Commercial Code (UCC), pursuant to which a bank would have been strictly liable for accepting forged checks had a complaint been filed within the three-year statute of limitations, preempted a common law negligence claim brought by a dentist and his professional association against the bank arising out of the bank's acceptance of checks payable to the professional association, on which an office manager had forged the dentist's indorsements for deposit into personal accounts of the manager and a dental hygienist; Article 3 provided the sole remedies available for the processing of checks with forged indorsements unless the parties had special relationship created by agreement, undertaking, or contract, and the plaintiffs complaint did not allege that they had a bank account at the bank, much less a special relationship. [N.J. Stat. Ann. §§ 12A:3-118\(g\), 12A:3-420. Lembo v. Marchese, 242 N.J. 477, 231 A.3d 735, 102 U.C.C. Rep. Serv. 2d 104 \(2020\).](#)

[END OF SUPPLEMENT]

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [Price v. Neal, 1762 WL 109 \(K.B. 1762\).](#)

² [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-418:1 \(3d ed.\).](#)

³ Former U.C.C. § 3-418.

⁴ [U.C.C. § 3-418 \(2002 Rev\), Official Comment 1.](#)

⁵ [U.C.C. § 3-418\(a\) \(2002 Rev\).](#)

⁶ [U.C.C. § 3-418\(c\) \(2002 Rev\).](#)

⁷ [§ 360.](#)

⁸ [Decibel Credit Union v. Pueblo Bank & Trust Co., 996 P.2d 784, 43 U.C.C. Rep. Serv. 2d 941 \(Colo. App. 2000\).](#)

⁹ [Southland Health Services, Inc. v. Bank of Vernon, 887 F. Supp. 2d 1158 \(N.D. Ala. 2012\) \(applying Alabama law\).](#)

11 Am. Jur. 2d Bills and Notes § 365

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

B. Discharge of Obligation to Pay

2. Discharge by Payment

b. Recovery of Payments

(2) Where Signature is Forged or Unauthorized

§ 365. Recovery on negotiable instrument where indorsement is forged

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  433

Whereas in cases where the signature of the drawer of a check is forged, the drawee bank may not recover a payment made to a holder in due course or to one who has, in good faith, changed position in reliance on the payment,¹ in forged indorsement cases, the drawee can sue back up the collection stream and recover against the party who took the check from the forger.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [§ 360.](#)

² [Payroll Check Cashing v. New Palestine Bank](#), 401 N.E.2d 752, 28 U.C.C. Rep. Serv. 1421 (Ind. Ct. App. 1980).
As to transfer warranties, see §§ 468 to 480
As to recovery in forged check cases, see [§ 364](#).

11 Am. Jur. 2d Bills and Notes X C Refs.

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

[X. Discharge of Obligation](#)

[C. Discharge of Secondary Obligors](#)

[Topic Summary](#) | [Correlation Table](#)

Research References

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A.L.R. Library

A.L.R. Index, Bills and Notes

A.L.R. Index, Checks and Drafts

A.L.R. Index, Holder in Due Course

A.L.R. Index, Release or Discharge

A.L.R. Index, Uniform Commercial Code

West's A.L.R. Digest, Bills and Notes  439, 440

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 366

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

1. In General

§ 366. Discharge of secondary obligors, generally

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to release of principal obligor, generally, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

White and Summers, Uniform Commercial Code § 16-11 (5th ed.)

Forms

Forms relating to discharge of accommodation party, generally, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\) Search Query](#)]

The Uniform Commercial Code provision governing the discharge of secondary obligors¹ contains rules that are applicable when a secondary obligor is a party to an instrument.² These rules essentially parallel modern interpretations of the law of suretyship and guaranty that apply when a secondary obligor is not a party to an instrument.³ Like the law of suretyship and guaranty, the Code provision governing the discharge of secondary obligors⁴ provides secondary obligors with defenses that are not available to other parties to instruments.⁵ In the event that a situation is presented that is not resolved by the Article governing negotiable instruments,⁶ the resolution may be provided by the general law of suretyship because that law is

applicable unless displaced by provisions of the U.C.C.⁷

The U.C.C. provision relating to the discharge of secondary obligors applies to:⁸

- accommodation parties
- indorsers of notes who are not accommodation parties
- the drawer of a draft that is accepted by a party that is not a bank
- a person who indorses a check
- the rights of comakers of instruments, even when those comakers do not qualify as accommodation parties

Observation:

Payment of the underlying debt by an accommodation party does not discharge the paper, nor does it relieve the accommodated party from liability under the note.⁹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605](#) (2002 Rev).

² [U.C.C. § 3-605](#) (2002 Rev), Official Comment 1.
A “secondary obligor” is defined in [§ 369](#).

³ [U.C.C. § 3-605](#) (2002 Rev), Official Comment 1.

⁴ [U.C.C. § 3-605](#) (2002 Rev).

⁵ [U.C.C. § 3-605](#) (2002 Rev), Official Comment 2.
As to parties to instruments, see §§ [50](#) to [74](#).

⁶ [U.C.C. §§ 3-101 to 3-605](#).

⁷ [U.C.C. § 3-605](#) (2002 Rev), Official Comment 1.

⁸ [U.C.C. § 3-605](#) (2002 Rev), Official Comments 2, 3.

⁹ [In re TML, Inc.](#), 291 B.R. 400, 50 U.C.C. Rep. Serv. 2d 511 (Bankr. W.D. Mich. 2003) (applying Michigan law).

11 Am. Jur. 2d Bills and Notes § 367

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

1. In General

§ 367. No discharge of secondary obligor who consents to event causing discharge or waives discharge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to preservation of rights, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

A secondary obligor is not discharged if the secondary obligor consents to the event or conduct that is the basis of the discharge, or the instrument or a separate agreement of the party provides for waiver of discharge, specifically referencing the Uniform Commercial Code provision governing the discharge of secondary obligors¹ or by general language indicating that the parties waive defenses based on suretyship or impairment of collateral.²

Unless the circumstances indicate otherwise, consent by the principal obligor to an act that would lead to a discharge under the Code provision governing the discharge of secondary obligors³ constitutes consent to that act by the secondary obligor if the secondary obligor controls the principal obligor or deals with the person entitled to enforce the instrument on behalf of the principal obligor.⁴

Comment:

It is standard practice to include such a waiver of suretyship defenses in notes prepared by financial institutions or other

commercial creditors.⁵ Thus, the Code provision governing the discharge of secondary obligors⁶ will result in the discharge of an accommodation party on a note only in the occasional case in which the note does not include such a waiver clause and the person entitled to enforce the note nevertheless takes actions that would give rise to a discharge under the code provision without obtaining the consent of the secondary obligor.⁷

Caution:

Because the foregoing provision⁸ by its terms applies only to a discharge “under this section,” it does not operate to waive a defense created by other law, such as the law governing enforcement of security interests under Revised U.C.C. Article 9,⁹ that cannot be waived under such other law.¹⁰

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605](#) (2002 Rev).

² [U.C.C. § 3-605\(f\)](#) (2002 Rev).
As to discharge by impairment of collateral, see §§ [379](#) to [383](#).

³ [U.C.C. § 3-605](#) (2002 Rev).

⁴ [U.C.C. § 3-605\(f\)](#) (2002 Rev).

⁵ [U.C.C. § 3-605\(f\)](#) (2002 Rev), Official Comment 9.

The provision of a line-of-credit note stating that the borrower waived various defenses and would not be released by any “extension” did not authorize a bank to hold the comaker or guarantor liable for the extension of additional amounts after the maturity date of the note, but rather merely eliminated the surety defense for an “extension” of the due date. [First of America Bank-Illinois, N.A. v. Drum](#), [295 Ill. App. 3d 205](#), [229 Ill. Dec. 714](#), [692 N.E.2d 703](#) (4th Dist. 1998).

⁶ [U.C.C. § 3-605](#) (2002 Rev).

⁷ [U.C.C. § 3-605\(f\)](#) (2002 Rev), Comment 9.

⁸ [U.C.C. § 3-605\(f\)](#) (2002 Rev).

⁹ [U.C.C. §§ 9-101 to 9-809](#).

¹⁰ [U.C.C. § 3-605\(f\)](#) (2002 Rev), Official Comment 9.

11 Am. Jur. 2d Bills and Notes § 368

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

1. In General

§ 368. Burden of persuasion on secondary obligor asserting discharge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to waiver and estoppel and U.C.C. 3-605A [Rev], see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

With one exception, a secondary obligor asserting discharge has the burden of persuasion both with respect to the occurrence of the acts alleged to harm the secondary obligor and loss or prejudice caused by those acts.¹

The one exception states that if the secondary obligor demonstrates prejudice caused by an impairment of its recourse, and the circumstances of the case indicate that the amount of loss is not reasonably susceptible of calculation or requires proof of facts that are not ascertainable, it is presumed that the act impairing recourse caused a loss or impairment equal to the liability of the secondary obligor on the instrument.² In that event, the burden of persuasion as to any lesser amount of the loss is on the person entitled to enforce the instrument.³

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(h\)](#) (2002 Rev).

² [U.C.C. § 3-605\(i\)](#) (2002 Rev).

³

[U.C.C. § 3-605\(i\)](#) (2002 Rev).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 369

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 369. Release of principal obligor on instrument; effect on principal obligor's duties to secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to release of the principal obligor, generally, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

If a person entitled to enforce an instrument releases the obligation of a principal obligor in whole or in part, and another party to the instrument is a secondary obligor, any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected. Unless the terms of the release preserve the secondary obligor's recourse, the principal obligor is discharged, to the extent of the release, from any other duties to the secondary obligor under Uniform Commercial Code Revised Article 3—Negotiable Instruments.¹

Definitions:

A "principal obligor," with respect to an instrument, means the accommodated party or any other party to the instrument against whom a secondary obligor has recourse under U.C.C. §§ 3-101 et seq.²

A "secondary obligor," with respect to an instrument, means an indorser or an accommodation party, a drawer having certain obligations, or any other party to the instrument that has a right of contribution against another party to the instrument.³

Comment:

The discharge of a principal obligor's duties to the secondary obligor is broad, applying to all duties under U.C.C. Revised Article 3—Negotiable Instruments.⁴ This includes not only the principal obligor's liability as a party to an instrument as a maker, drawer, or indorser, but also obligations for joint and several liability, contribution, and as an accommodation party.⁵

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(a)(1) (2002 Rev), referring to U.C.C. §§ 3-101 to 3-605.

² U.C.C. § 3-103(a)(11) (2002 Rev).

³ U.C.C. § 3-103(a)(17) (2002 Rev).

⁴ U.C.C. §§ 3-101 to 3-605.

⁵ U.C.C. § 3-605 (2002 Rev), Official Comment 4.
As to the liability of various parties, see §§ 386 to 493.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 370

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 370. Release of principal obligor on instrument; effect on principal obligor's duties to secondary obligor—Discharge of secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to release of the principal obligor, generally, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

If a person entitled to enforce an instrument releases the obligation of a principal obligor in whole or in part, and another party to the instrument is a secondary obligor, unless the terms of the release provide that the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor, the secondary obligor is discharged to the same extent as the principal obligor from any unperformed portion of its obligation on the instrument.¹ If the instrument is a check and the obligation of the secondary obligor is based on an indorsement of the check, the secondary obligor is discharged without regard to the language or circumstances of the discharge or other release.²

If the secondary obligor is not discharged as stated above, the secondary obligor is discharged to the extent of the value of the consideration for the release, and to the extent that the release would otherwise cause the secondary obligor a loss.³

Comments:

The discharge of the secondary obligor is phrased more narrowly than the discharge of the principal obligor because, unlike

principal obligors, the only obligations of secondary obligors in Uniform Commercial Code Revised Article 3—Negotiable Instruments⁴ are on the instrument as makers or indorsers.⁵

The parties can opt out of this rule by including a contrary statement in the terms of the release; no “magic words” are necessary.⁶ Thus, discharge of the secondary obligor is avoided not only if the terms of the release track the statutory language (e.g., the person entitled to enforce the instrument “retains the right to enforce the instrument” against the secondary obligor), or if the terms of the release effect a preservation of recourse,⁷ but also if the terms of the release include a simple statement that the parties intend to “release the principal obligor but not the secondary obligor” or that the person entitled to enforce the instrument “reserves its rights” against the secondary obligor.⁸ At the same time, because this provision refers to the “terms of the release,” extrinsic circumstances cannot be used to establish that the parties intended the secondary obligor to remain obligated. If a release of the principal obligor includes such a provision, the secondary obligor is, nonetheless, discharged to the extent of the consideration that is paid for the release; that consideration is treated as a payment in partial satisfaction of the instrument.⁹

Caution:

Secondary obligors cannot obtain a discharge in any transaction in which they have consented to the challenged conduct.¹⁰ Thus, the above rules will not apply to any transaction that includes a provision waiving suretyship defenses (a provision that is almost universally included in commercial loan documentation) or to any transaction in which the creditor obtains the consent of the secondary obligor at the time of the release.¹¹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(a)(2) (2002 Rev).

² U.C.C. § 3-605(a)(2) (2002 Rev).

³ U.C.C. § 3-605(a)(3) (2002 Rev).

⁴ U.C.C. §§ 3-101 to 3-605.

⁵ U.C.C. § 3-605 (2002 Rev), Official Comment 4.

⁶ U.C.C. § 3-605 (2002 Rev), Official Comment 4.

⁷ As to preservation of recourse of a secondary obligor, see § 375.

⁸ U.C.C. § 3-605 (2002 Rev), Official Comment 4.

⁹ U.C.C. § 3-605 (2002 Rev), Official Comment 4.

¹⁰ § 367.

¹¹ U.C.C. § 3-605 (2002 Rev), Official Comment 4.

§ 370. Release of principal obligor on instrument; effect..., 11 Am. Jur. 2d Bills...

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 371

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 371. Release of principal obligor on instrument; effect on principal obligor's duties to secondary obligor—No discharge of secondary obligor without notice or knowledge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A secondary obligor is not discharged to the extent of the value of the consideration for the release, and to the extent that the release would otherwise cause the secondary obligor a loss¹ unless the person entitled to enforce the instrument knows that the person is a secondary obligor or has notice that the instrument was signed for accommodation.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [§ 370.](#)

² [U.C.C. § 3-605\(e\)](#) (2002 Rev).

11 Am. Jur. 2d Bills and Notes § 372

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 372. Extension of due date of obligation on instrument; effect of extension of due date of obligation on principal obligor's duties to secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to extensions, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments
[\[Westlaw®\(r\): Search Query\]](#)

Forms

Forms relating to extension, generally, see Am. Jur. Legal Forms 2d, Uniform Commercial Code; Am. Jur. Pleading and Practice Forms, Commercial Code [\[Westlaw®\(r\) Search Query\]](#)

If a person entitled to enforce an instrument grants a principal obligor an extension of the time at which one or more payments are due and another party to the instrument is a secondary obligor, any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected.¹ Thus, the secondary obligor may recover from the principal obligor for any payments the secondary obligor already made to the holder.²

Unless the terms of the extension preserve the secondary obligor's recourse, the extension correspondingly extends the time

for performance of any other duties owed to the secondary obligor by the principal obligor under Uniform Commercial Code Revised Article 3—Negotiable Instruments.³

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(b\)\(1\)](#) (2002 Rev).

² [Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-605A:5 \[Rev.\] \(3d ed.\)](#).

³ [U.C.C. § 3-605\(b\)\(1\)](#) (2002 Rev), referring to [U.C.C. §§ 3-101 to 3-605](#).

As to the effect of a renewal of an instrument on the liability of nonconsenting comakers, see [§ 172](#).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 373

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 373. Extension of due date of obligation; effect of extension of due date of obligation on principal obligor's duties to secondary obligor—Discharge of secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to extensions, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments
[Westlaw®(r): Search Query]

If a person entitled to enforce an instrument grants a principal obligor an extension of the time at which one or more payments are due on the instrument and another party to the instrument is a secondary obligor, the secondary obligor is discharged to the extent that the extension would otherwise cause the secondary obligor a loss.¹

Comment:

In some cases, the extension may cause loss to the secondary obligor, particularly if deterioration of the financial condition of the principal obligor reduces the amount that the secondary obligor is able to recover on its right of recourse when default occurs. For example, suppose that the instrument is an installment note and the principal debtor is temporarily short of funds to pay a monthly installment. The payee agrees to extend the due date of the installment for a month or two to allow the debtor to pay when funds are available. The above rule provides that an extension of time results in a discharge of the secondary obligor, but only to the extent that the secondary obligor proves that the extension caused loss. Thus, if the extension is for a long period, the secondary obligor might be able to prove that during the period of extension the principal obligor became insolvent, reducing the value of the

right of recourse of the secondary obligor. In such a case, the above rule discharges the secondary obligor to the extent of that harm. Although not required to notify the secondary obligor of the extension, the payee can minimize the risk of loss by the secondary obligor by giving the secondary obligor prompt notice of the extension; prompt notice can enhance the likelihood that the secondary obligor's right of recourse can remain valuable, and thus can limit the likelihood that the secondary obligor will suffer a loss because of the extension.²

To the extent that the secondary obligor is not discharged as stated above, the secondary obligor may perform its obligations to a person entitled to enforce the instrument as if the time for payment had not been extended or, unless the terms of the extension provide that the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor as if the time for payment had not been extended, treat the time for performance of its obligations as having been extended correspondingly.³

Comments:

As a practical matter, an extension of the due date will normally occur only when the principal obligor is unable to pay on the due date. The interest of the secondary obligor normally is to acquiesce in the willingness of the person entitled to enforce the instrument to wait for payment from the principal obligor rather than to pay right away and rely on an action against the principal obligor that may have little or no value. In contrast, in unusual cases the secondary obligor may prefer to pay the holder on the original due date so as to avoid continuing accrual of interest. In such cases, the secondary obligor may do so.⁴

If the terms of the extension provide that the person entitled to enforce the instrument retains its right to enforce the instrument against the secondary obligor on the original due date, though, those terms are effective and the secondary obligor may not delay payment until the extended due date.⁵

Unless the extension agreement effects a preservation of recourse,⁶ however, the secondary obligor may not proceed against the principal obligor as the signer of an accommodation instrument until the extended due date. To the extent that delay causes loss to the secondary obligor, it is discharged.⁷

Even in those cases in which a secondary obligor does not have a duty to pay the instrument on the original due date, it always has the right to pay the instrument on that date, and perhaps minimize its loss by doing so. The secondary obligor is not precluded, however, from asserting its rights to discharge if it does not exercise that option. The critical issue is whether the extension caused the secondary obligor a loss by increasing the difference between its cost of performing its obligation on the instrument and the amount recoverable from the principal obligor under U.C.C. §§ 3-101 et seq. The decision by the secondary obligor not to exercise its option to pay on the original due date may, under the circumstances, be a factor to be considered in the determination of that issue, especially if the secondary obligor has been given prompt notice of the extension.⁸

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(b)(2) (2002 Rev).
As to renewal or novation as a basis for discharge of an obligation, generally, see § 350.

² U.C.C. § 3-605 (2002 Rev), Official Comment 5.

³ U.C.C. § 3-605(b)(3) (2002 Rev).

⁴ U.C.C. § 3-605 (2002 Rev), Official Comment 5.

⁵ U.C.C. § 3-605 (2002 Rev), Official Comment 5.

⁶ § 375.

⁷ U.C.C. § 3-605 (2002 Rev), Official Comment 5.

⁸ U.C.C. § 3-605 (2002 Rev), Official Comment 5.

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 374

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 374. Extension of due date of obligation; effect of extension of due date of obligation on principal obligor's duties to secondary obligor—No discharge of secondary obligor without notice or knowledge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A secondary obligor is not discharged where an extension is granted to the principal obligor¹ unless the person entitled to enforce the instrument knows that the person is a secondary obligor or has notice that the instrument was signed for accommodation.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ §§ 372, 373.

² U.C.C. § 3-605(e) (2002 Rev).

11 Am. Jur. 2d Bills and Notes § 375

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 375. Preservation of secondary obligor's right to recourse after release or extension

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to preservation of rights, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\) Search Query](#)]

Forms

Forms relating to reservation or nonimpairment of rights, see Am. Jur. Legal Forms 2d, Bills and Notes; Am. Jur. Legal Forms 2d, Uniform Commercial Code [[Westlaw®\(r\) Search Query](#)]

A release or extension preserves a secondary obligor's recourse if the terms of the release or extension provide that:¹

- (1) the person entitled to enforce the instrument retains the right to enforce the instrument against the secondary obligor; and
- (2) the recourse of the secondary obligor continues as if the release or extension had not been granted.

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(g\)](#) (2002 Rev).

As to discharges by release, see §§ [369](#) to [371](#).

As to discharges by reason of extensions of time, see §§ [372](#) to [374](#).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 376

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 376. Modification of principal obligor's obligation; effect of modification on principal obligor's duties to secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to modifications, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments
[\[Westlaw®\(r\): Search Query\]](#)

If a person entitled to enforce an instrument agrees, with or without consideration, to a modification of the obligation of a principal obligor, other than a complete or partial release or an extension of the due date, and another party to the instrument is a secondary obligor, any obligations of the principal obligor to the secondary obligor with respect to any previous payment by the secondary obligor are not affected. The modification correspondingly modifies any other duties owed to the secondary obligor by the principal obligor under Uniform Commercial Code Revised Article 3—Negotiable Instruments.¹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(c\)\(1\)](#) (2002 Rev), referring to [U.C.C. §§ 3-101 to 3-605](#).

As to discharges by release, see §§ [369](#) to [371](#).

As to discharges by reason of extensions of time, see §§ [372](#), [373](#), [374](#).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 377

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 377. Effect of modification on principal obligor's duties to secondary obligor; discharge of secondary obligor

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to modifications, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments
[\[Westlaw®\(r\): Search Query\]](#)

If a person entitled to enforce an instrument agrees, with or without consideration, to a modification of the obligation of a principal obligor, other than a complete or partial release or an extension of the due date, and another party to the instrument is a secondary obligor, the secondary obligor is discharged from any unperformed portion of its obligation to the extent that the modification would otherwise cause the secondary obligor a loss.¹

To the extent that the secondary obligor is not discharged as provided above, the secondary obligor may satisfy its obligation on the instrument as if the modification had not occurred, or treat its obligation on the instrument as having been modified correspondingly.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(c\)\(2\)](#) (2002 Rev.).

As to discharges by release, see §§ [369](#) to [371](#).

As to discharges by reason of extensions of time, see §§ [372](#) to [374](#).

² [U.C.C. § 3-605\(c\)\(3\)](#) (2002 Rev).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 378

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

2. Discharge by Impairment of Recourse

§ 378. Effect of modification on principal obligor's duties to secondary obligor; discharge of secondary obligor—No discharge of secondary obligor without notice or knowledge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A secondary obligor is not discharged under the Code provision governing the effect of certain modifications on a secondary obligor,¹ unless the person entitled to enforce the instrument knows that the person is a secondary obligor or has notice that the instrument was signed for accommodation.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ §§ 376, 377.

² U.C.C. § 3-605(e) (2002 Rev).

11 Am. Jur. 2d Bills and Notes § 379

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

3. Discharge by Impairment of Collateral

§ 379. Discharge of secondary obligor upon impairment of collateral, generally

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A.L.R. Library

What constitutes unjustifiable impairment of collateral, discharging parties to a negotiable instrument under U.C.C. sec. 3-606(1)(b), 61 A.L.R.5th 525

Who is "party" discharged on negotiable instrument to extent of holder's unjustifiable impairment of collateral, under U.C.C. sec. 3-606(1)(b), 93 A.L.R.3d 1283

Treatises and Practice Aids

As to impairment of collateral, generally, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to impairment of collateral, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\)](#)]

[Search Query]

If the obligation of a principal obligor is secured by an interest in collateral, another party to the instrument is a secondary obligor with respect to that obligation, and a person entitled to enforce the instrument impairs the value of the interest in collateral, the obligation of the secondary obligor is discharged to the extent of the impairment.¹

Impairing the value of an interest in collateral includes:²

- failure to obtain or maintain perfection or recordation of the interest in collateral³
- release of collateral without substitution of collateral of equal value or equivalent reduction of the underlying obligation⁴
- failure to perform a duty to preserve the value of collateral owed, under Uniform Commercial Code Revised Article 9—Secured Transactions⁵ or other law, to a debtor or other person secondarily liable⁶
- failure to comply with applicable law in disposing of or otherwise enforcing the interest in collateral⁷

Because the code provision governing the effect of the impairment of collateral⁸ uses the term “includes,” it allows a court to find impairment in other cases as well.⁹

Comment:

This provision applies whether the collateral is personalty or realty, whenever the obligation in question is in the form of a negotiable instrument.¹⁰

Observation:

The 2002 Amendment to the code provision governing the effect of the impairment of collateral¹¹ represents no substantive change from the 1990 version (former U.C.C. § 3-605(e)).¹² Thus, caselaw from the previous statute regarding impairment of collateral is still valid.

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(d) (2002 Rev).

² U.C.C. § 3-605(d) (2002 Rev).

³ § 381.

⁴ § 381.

⁵ U.C.C. § 9-101 to 9-809.

⁶ § 382.

As to a secured party's duty to preserve collateral under [U.C.C. §§ 9-101 et seq.](#), see [Am. Jur. 2d, Secured Transactions §§ 404 to 417](#).

⁷ As to improper disposition of collateral, see [§ 382](#).

⁸ [U.C.C. § 3-605\(d\)](#) (2002 Rev).

⁹ [U.C.C. § 3-605\(d\)](#) (2002 Rev), Official Comment 7.

¹⁰ [U.C.C. § 3-605\(d\)](#) (2002 Rev), Official Comment 7.

¹¹ [U.C.C. § 3-605\(d\)](#) (2002 Rev).

¹² Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-605A:19 [Rev.] (3d ed.).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 380

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

3. Discharge by Impairment of Collateral

§ 380. Discharge of secondary obligor upon impairment of collateral, generally—Extent of impairment

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to measurement of impairment, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

The value of an interest in collateral is impaired to the extent the value of the interest is reduced to an amount less than the amount of the recourse of the secondary obligor, or the reduction in value of the interest causes an increase in the amount by which the amount of the recourse exceeds the value of the interest.¹ However, if it is shown that the collateral was worthless, there can be no unjustifiable impairment.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [U.C.C. § 3-605\(d\)](#) (2002 Rev).

² [Lyons v. Citizens Commercial Bank of Tallahassee](#), 443 So. 2d 229, 37 U.C.C. Rep. Serv. 1214 (Fla. 1st DCA 1983). Where the value of an airplane destroyed in a crash was only \$1,000, the creditor's release of its lien on the aircraft in exchange for a payment in that amount did not constitute impairment of collateral. [U.S. v. Unum, Inc.](#), 658 F.2d 300, 32 U.C.C. Rep. Serv. 646 (5th Cir. 1981).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 381

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

3. Discharge by Impairment of Collateral

§ 381. Discharge of secondary obligor upon impairment of collateral, generally—By failure to perfect, or by release of, security interest

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to specific acts of impairment, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Forms

Forms relating to impairment of collateral, see Am. Jur. Pleading and Practice Forms, Commercial Code [[Westlaw®\(r\): Search Query](#)]

Impairment of the value of an interest in collateral, such as will discharge the obligation of an accommodation party or indorser, includes a failure to obtain or maintain perfection or recordation of the interest in collateral.¹

A creditor's unreasonable failure to perfect its purchase money security interest in distribution rights that it has sold to the debtor by filing a financing statement in a timely manner, as a result of which a preexisting lien covering the distribution rights that is held by a bank takes priority over the interest of the creditor, effectively releases the collateral and discharges

the guarantor of the promissory note used to finance the purchase.² However, a holder's failure to record a note does not constitute unjustifiable impairment of collateral, relieving an accommodation indorser of any further obligation on the note, since the recording of a promissory note would not convert it into security interest in the obligor's property.³

Comment:

Assume, for example, that the payee of a secured note fails to perfect the security interest. The collateral is owned by the principal obligor who subsequently files in bankruptcy. As a result of the failure to perfect, the security interest is not enforceable in bankruptcy. If the payee were to obtain payment from the secondary obligor, the secondary obligor would be subrogated to the payee's security interest in the collateral. In this situation, though, the value of the security interest is impaired completely because the security interest is unenforceable. Thus, the secondary obligor is discharged from its obligation on the note to the extent of that impairment. If the value of the collateral impaired is as much or more than the amount of the note, and if there will be no recovery on the note as an unsecured claim, there is a complete discharge.⁴

A person also impairs the value of an interest in collateral by releasing the collateral without substitution of collateral of equal value or equivalent reduction of the underlying obligation.⁵ Thus, for example, where a bank releases collateral under a security agreement without the consent of an indorser of the secured notes, and the value of the released collateral would have been sufficient to satisfy the outstanding indebtedness represented by the notes, the bank cannot recover against the indorser.⁶

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(d) (2002 Rev).

² *Port Distributing Corp. v. Pflaumer*, 880 F. Supp. 204, 28 U.C.C. Rep. Serv. 2d 235 (S.D. N.Y. 1995), judgment aff'd, 70 F.3d 8, 28 U.C.C. Rep. Serv. 2d 248 (2d Cir. 1995).

An individual's wholly owned corporation was not a party to a deed of trust note executed by the individual in conjunction with the purchase of a hotel, and thus could not invoke impairment of collateral as a defense to a suit seeking to foreclose on its property which had been pledged as additional security to satisfy the balance of the debt, regardless of whether or not the holder had impaired any collateral for the note by failing to properly perfect a security agreement covering personal property of the hotel. *D.R. Allen & Son, Inc. v. Harwal, Inc.*, 307 S.C. 315, 414 S.E.2d 805, 17 U.C.C. Rep. Serv. 2d 1199 (Ct. App. 1992).

Although a bank's failure to perfect a purchase money security interest in collateral given to secure a note by properly filing a financing statement was an unjustifiable impairment of collateral, the persons asserting a discharge by reason of the impairment were not entitled to be discharged since they signed the note as makers rather than as accommodation parties. *Peoples Bank of Point Pleasant v. Pied Piper Retreat, Inc.*, 158 W. Va. 170, 209 S.E.2d 573, 14 U.C.C. Rep. Serv. 1398 (1974).

³ *First State Bank of Ocean County v. Raiton*, 377 F. Supp. 859, 15 U.C.C. Rep. Serv. 420 (E.D. Pa. 1974).

⁴ U.C.C. § 3-605 (2002 Rev), Official Comment 7.

⁵ U.C.C. § 3-605(d) (2002 Rev).

⁶ *Guida v. Exchange Nat. Bank of Tampa*, 308 So. 2d 148, 16 U.C.C. Rep. Serv. 1062 (Fla. 2d DCA 1975).

Works.

11 Am. Jur. 2d Bills and Notes § 382

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

3. Discharge by Impairment of Collateral

§ 382. Discharge of secondary obligor upon impairment of collateral, generally—By failure to preserve value or improper disposition

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

Treatises and Practice Aids

As to failure to preserve value or improper disposition of collateral, see Lawrence's Anderson on the Uniform Commercial Code, Article 3 [Rev] Negotiable Instruments [[Westlaw®\(r\): Search Query](#)]

Impairment of the value of an interest in collateral such as will discharge the obligation of an accommodation party or indorser includes the failure to perform a duty owed, under Uniform Commercial Code Revised Article 9—Secured Transactions¹ or other law, to preserve the value of collateral to a debtor or other person secondarily liable.²

Unless otherwise agreed, where the collateral is property in the possession of the person entitled to enforce the instrument, he or she has the duty to use reasonable care in its custody and possession.³

Impairment of the value of an interest in collateral also includes a failure to comply with applicable law in disposing of or otherwise enforcing the interest in the collateral.⁴ In the case of a secured transaction under Uniform Commercial Code Revised Article 9—Secured Transactions,⁵ a failure to dispose of collateral in the manner required by statute⁶ will result in an impairment of the collateral.⁷

Footnotes

¹ U.C.C. § 9-101 to 9-809.

² U.C.C. § 3-605(d) (2002 Rev).

³ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-605:21 [Rev.] (3d ed.).
As to a secured party's duty to preserve collateral under U.C.C. §§ 9-101 et seq., see Am. Jur. 2d, Secured Transactions §§ 404 to 417.

⁴ U.C.C. § 3-605(d) (2002 Rev).

⁵ U.C.C. §§ 9-101 to 9-809.

⁶ U.C.C. § 9-610.

As to a secured creditor's right to dispose of collateral, see Am. Jur. 2d, Secured Transactions §§ 491 to 500.

⁷ Frisch, Lawrence's Anderson on the Uniform Commercial Code § 3-605:22 [Rev.] (3d ed.).

End of Document

© 2021 Thomson Reuters. No claim to original U.S. Government Works.

11 Am. Jur. 2d Bills and Notes § 383

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

3. Discharge by Impairment of Collateral

§ 383. Discharge of secondary obligor upon impairment of collateral, generally—No discharge without notice or knowledge

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes  439, 440

A secondary obligor is not discharged under the code provision governing the effect of the impairment of collateral¹ unless the person entitled to enforce the instrument knows that the person is a secondary obligor or has notice that the instrument was signed for accommodation.²

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ U.C.C. § 3-605(d) (2002 Rev), discussed in §§ 379 to 383.

² U.C.C. § 3-605(e) (2002 Rev).

11 Am. Jur. 2d Bills and Notes § 384

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

4. Particular Applications

§ 384. Cases where discharge of secondary obligor warranted

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes 439, 440

Where the payee of a note accepts a maker's postdated check and extends the time of payment from the date the note became delinquent until the date when the check is payable, and where the extension of time is granted without notice to or consent of the accommodation parties to the note, the accommodation parties are relieved of further liability on the note.¹ Likewise, the increase in the risk of nonpayment of a promissory note executed by a purchaser in connection with the purchase of an apartment building which results from the seller's subordination of the purchaser's second deed of trust to a fourth deed of trust executed by subsequent buyers of the building is an impairment of collateral; the original purchaser becomes, in effect, a surety on the subsequent buyers' note by reason of the subordination and is entitled to be discharged because the risk of nonpayment has been increased without consent.² Similarly, in a suit by the holder of a note given for the purchase of realty against an individual who was the original purchaser of the realty and the original maker of the note prior to its assumption by a third party under a novation, the original maker of the note is a surety entitled to protection from harmful impairment of the note's collateral; the holder of note unreasonably impairs the value of its collateral by executing a subordination agreement and releasing over 700 acres of the land which constitutes collateral, without the surety's knowledge, and the surety is discharged by the impairment from liability on the note.³

A bank which is named payee under a loss payable clause in a breach of warranty insurance policy procured by a maker impairs the value of collateral by failing to pursue a potential claim for available insurance coverage which could reduce or eliminate the amount due on the note.⁴ Where a bank negligently fails to perfect its security interest in a growing corn crop by omitting a description of the real estate as required by statute thereby causing said collateral to be subordinated to the interest of a third party, there is, likewise, an unjustifiable impairment of collateral which serves to discharge an accommodation party from liability to the extent of the impairment.⁵ Similarly, in a creditor's suit against the guarantor of a note secured by a mortgage on the debtor's realty, the creditor's failure to record the mortgage for one year impairs both the value of the collateral and the guarantor's right as surety to be subrogated to all of the creditor's rights against the debtor, including the right to proceed against any security of the debtor in the creditor's hands.⁶

An accommodation party is totally discharged by a secured creditor's impairment of collateral where the collateral, although not in the possession of the creditor, is sold by the principal debtor with the express authority of the secured creditor and where the value of the collateral exceeds the amount of the debt.⁷

In a suit by a payee as holder of a note executed by a husband and wife as debtors, which is secured by a security interest in the inventory of the husband's business, the wife is discharged from liability on the note to the extent of the collateral's value by reason of the payee's failure to timely perfect the security interest in the inventory since:⁸

- (1) the impairment-of-collateral provision of the U.C.C. applies to all parties who occupy the position of surety, including accommodation makers, comakers, endorsers, guarantors, and acceptors;
- (2) the wife is an accommodation comaker of the note in question because she signed it as an accommodation to her husband to enable him to get a loan and has not received any direct benefit from the loan;
- (3) the lender had notice of the wife's accommodation status; and
- (4) the lender's failure to perfect its security interest in the collateral for the note, which has resulted in the loss of the entire collateral to another secured party, constitutes unjustifiable impairment of collateral.

Where an automobile dealer assigns and indorses a contract of sale and note to a bank, together with an insurance policy which is itself collateral for the note, and the bank fails either to replace the policy when it is cancelled or to notify the dealer of the policy's cancellation, the bank has impaired the collateral and the dealer's liability as an indorser is thereby discharged.⁹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ Lee Federal Credit Union v. Gussie, 542 F.2d 887, 19 U.C.C. Rep. Serv. 630 (4th Cir. 1976).

² Haberl v. Bigelow, 855 P.2d 1368, 23 U.C.C. Rep. Serv. 2d 820 (Colo. 1993).

³ Hughes v. Tyler, 485 So. 2d 1026, 42 U.C.C. Rep. Serv. 1699 (Miss. 1986).

⁴ Darien Bank v. Miller, 208 Ga. App. 562, 431 S.E.2d 165 (1993).

⁵ Estate of Voelker, 252 N.W.2d 400, 21 U.C.C. Rep. Serv. 817 (Iowa 1977).

⁶ Langeveld v. L.R.Z.H. Corp., 74 N.J. 45, 376 A.2d 931, 22 U.C.C. Rep. Serv. 106, 95 A.L.R.3d 949 (1977) (also holding that if the impairment of collateral can be measured in monetary terms, the monetary amount of the impairment will measure the extent of the guarantor's discharge from liability on a note, but if the monetary amount of impairment cannot be ascertained the guarantor will be discharged of all liability on the instrument).

⁷ Beneficial Finance Co. of Norman v. Marshall, 1976 OK CIV APP 10, 551 P.2d 315, 18 U.C.C. Rep. Serv. 1014 (Ct. App. Div. 1 1976).

⁸ El-Ce Storms Trust v. Svetahor, 223 Mont. 113, 724 P.2d 704, 2 U.C.C. Rep. Serv. 2d 1593 (1986) (also holding that, since the wife was still liable on the note as a comaker, she was obligated to pay the amount of the plaintiff's judgment, less the value of the collateral for the note).

⁹ Arlington Bank and Trust v. Nowell Motors, Inc., 511 S.W.2d 415, 15 U.C.C. Rep. Serv. 146 (Tex. Civ. App. Fort Worth 1974).

11 Am. Jur. 2d Bills and Notes § 385

American Jurisprudence, Second Edition | May 2021 Update

Bills and Notes

Lonnie E. Griffith, Jr., J.D.; Sonja Larsen, J.D.; Lucas Martin, J.D.; Karl Oakes, J.D.; Eric C. Surette, J.D.; and Barbara J. Van Arsdale, J.D.

X. Discharge of Obligation

C. Discharge of Secondary Obligors

4. Particular Applications

§ 385. Cases where discharge of secondary obligor not warranted

[Topic Summary](#) | [Correlation Table](#) | [References](#)

West's Key Number Digest

West's Key Number Digest, Bills and Notes 439, 440

A first lender is entitled to recover the full amount of a promissory note from borrowers despite the colender's notation on the note that the debt was "paid in full," where the note is payable to both lenders, and the colender thus cannot discharge or release the interest of the first lender in the note without the first lender's consent.¹

The fact that a predecessor of the Resolution Trust Corporation (RTC) has orally agreed, without a general partner's consent, not to file suit on notes given by a partnership does not release the general partner from liability on a judgment against the partnership and other partners, since unwritten agreements tending to defeat or diminish RTC's rights under an instrument are unenforceable against the RTC; moreover, the general partner in such a case is not a surety known to the creditor, even if he is considered to be a latent surety, and the section of the Uniform Commercial Code (U.C.C.) which deals with discharge of a party to an instrument because of a holder's release of rights against a third party² protects only known sureties.³ Likewise, where a bank which holds a partnership note is informed two or three days before the note is due that one partner is buying the other partner's interest and is assuming all liabilities of the business and that the withdrawing partner does not want the note extended and will not sign a renewal note, evidence that bank twice accepts payment of interest from the continuing partner after the note becomes due does not establish that the bank has made an enforceable promise not to sue the continuing partner; thus, the withdrawing partner is not discharged.⁴

An accommodation comaker of a note executed by her husband in favor of a bank cannot escape liability on the ground that the bank has unjustifiably impaired the value of collateral by listing the note as unsecured in the husband's bankruptcy proceeding, when in fact the note is secured, since the bank is not required to take affirmative action to enforce its security in the absence of any implied duty to do so.⁵ Moreover, an assignee of promissory notes has no duty to monitor the condition of motels administered by the sole general partner of a limited partnership; thus, no discharge for impairment of collateral is warranted, even though the condition of the motels has deteriorated during the time that the creditor has delayed foreclosure, resulting in a decrease in the fair market value of the collateral.⁶

Even if a creditor has forged the debtor's signature on a security agreement, that conduct does not increase a guarantor's liability under a guaranty agreement, and thus, does not impair collateral so as to discharge the guarantor's obligation, where the proceeds from the sale of the collateral are applied to the balance due on the notes, reducing the liability of the guarantors.⁷ Likewise, in an action against a guarantor who has advised the creditor to dispose of collateral over an extended period of time through a liquidator specially recommended by the guarantor, the fact that the creditor disregards that advice and sells the collateral at public auction for an amount less than the loan balance does not constitute an unjustifiable impairment of collateral, where the guarantor has waived its right to claim a discharge by consenting in its guaranty to an auction sale as an appropriate method for disposal of the collateral.⁸

Chapter 11 debtors could not assert an impairment defense to their liability under a promissory note where the debtors had signed the note, not as guarantors or accommodation parties, but as comakers.⁹

A promissory note maker's affirmative defense that a note holder's president had received funds from a lender in payment for the note is not supported by the evidence where neither holder nor maker is a party to the payment made to the president by the lender, and, thus, the note holder is still entitled to payment from the maker.¹⁰

A guarantor who unconditionally guarantees payment of a note and mortgage debt by a separate contract is not a party to the instrument, meaning the promissory note, because he has not signed the instrument; thus, the guaranty transaction is not within the scope of the impairment-of-collateral statute and the creditor's unjustified impairment of collateral for the note and mortgage will not cause the guarantor to be discharged from liability for payment of the sum guaranteed.¹¹

© 2021 Thomson Reuters. 33-34B © 2021 Thomson Reuters/RIA. No Claim to Orig. U.S. Govt. Works. All rights reserved.

Footnotes

¹ [Marshall v. Marshall](#), 73 A.D.3d 870, 905 N.Y.S.2d 182 (2d Dep't 2010).

² As to discharges by reason of impairment of a right of recourse, see §§ [369](#) to [378](#).

³ [Resolution Trust Corp. v. Teem Partnership](#), 835 F. Supp. 563, 22 U.C.C. Rep. Serv. 2d 1094 (D. Colo. 1993) (applying the pre-1990 version of the U.C.C., which was in effect in Colorado until the January 1, 1995, the effective date of the 1990 Revision).

⁴ [Glover v. National Bank of Commerce of Pine Bluff](#), 258 Ark. 771, 529 S.W.2d 333, 18 U.C.C. Rep. Serv. 459 (1975).

As to discharges by reason of extension, see §§ [372](#) to [374](#).

⁵ [Chemical Bank v. Valentini](#), 84 A.D.2d 801, 444 N.Y.S.2d 154, 32 U.C.C. Rep. Serv. 901 (2d Dep't 1981).

⁶ [Buckeye Fed. S. & L. Assn. v. Guirlinger](#), 62 Ohio St. 3d 312, 581 N.E.2d 1352, 16 U.C.C. Rep. Serv. 2d 432 (1991).

⁷ [First City, Texas-Beaumont, N.A. v. Treece](#), 848 F. Supp. 727, 25 U.C.C. Rep. Serv. 2d 161 (E.D. Tex. 1994). As to discharges by reason of impairment of collateral, see §§ [379](#) to [383](#).

⁸ [Rhode Island Hospital Trust Nat. Bank v. National Health Foundation](#), 119 R.I. 823, 384 A.2d 301, 23 U.C.C. Rep. Serv. 1237 (1978).

⁹ [In re Bahara](#), 219 B.R. 77, 35 U.C.C. Rep. Serv. 2d 1253 (M.D. Pa. 1998) (applying Pennsylvania law).

¹⁰ [Levitin v. Michael Group, L.L.C.](#), 277 S.W.3d 121 (Tex. App. Dallas 2009).

¹¹ [Crown Life Ins. Co. v. LaBonte](#), 111 Wis. 2d 26, 330 N.W.2d 201, 36 U.C.C. Rep. Serv. 1232 (1983).

